IN THE

Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-1544

JOYCE BEVERAGES, INC., JOHN M. JOYCE AND WILLIAM J. COLLIER,

Petitioners,

vs.

WILLIAM J. JOYCE, BERNICE RILEY JOYCE, MARY JOYCE HAMMOND, WILLIAM J. JOYCE, JR., DOROTHY ANN JOYCE, CATHERINE JOYCE McMANUS, PAUL McMANUS, JILL JOYCE KASSELMAN AND JUDITH JOYCE LANG,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR RESPONDENTS IN OPPOSITION.

DONALD E. EGAN,
LEE ANN WATSON,
KATTEN, MUCHIN, GITLES,
ZAVIS, PEARL & GALLER,
55 East Monroe Street,
Suite 4100,
Chicago, Illinois 60603,
(312) 346-7400,
Attorneys for Respondents.

Gunthorp-Warren Printing Company, Chicago • Financial 6-6565

INDEX.

TABLE OF AUTHORITIES.

Cases.

Statutes and Rules.

Treatises.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-1544.

JOYCE BEVERAGES, INC., JOHN M. JOYCE AND WILLIAM J. COLLIER,

Petitioners,

vs.

WILLIAM J. JOYCE, BERNICE RILEY JOYCE, MARY JOYCE HAMMOND, WILLIAM J. JOYCE, JR., DOROTHY ANN JOYCE, CATHERINE JOYCE McMANUS, PAUL McMANUS, JILL JOYCE KASSELMAN AND JUDITH JOYCE LANG,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR RESPONDENTS IN OPPOSITION.

OPINIONS BELOW.

The opinion of the Court of Appeals for the Second Circuit, which was not reported at the time the Petition was filed, is reported at 571 F. 2d 703 (2d Cir. 1978) (2a).[1]

1. Numbers in parenthesis followed by "a" refer to pages in the Appendix attached to the petitioners' brief.

QUESTION PRESENTED.[2]

Whether plaintiffs' Complaint states a claim upon which relief can be granted under the Securities Exchange Act of 1934 in alleging that a disclosure document accompanying a stock exchange offer to shareholders contained materially misleading statements with respect to the potential availability of Rule 144 and omitted certain material information with respect to changes in shareholders' rights which was necessary to make other statements not misleading?

STATEMENT OF THE CASE.

Contrary to Supreme Court Rule 40, much of the defendants' Statement of the Case is argumentative,[3] particularly in relation to the misleading statements upon which the plaintiffs base their claim. (Petition, pp. 7-9.) Such statements are clearly inappropriate in the Statement of the Case and accordingly will not be addressed by plaintiffs. Rather this Statement of the Case will be confined to a correction of the omissions and inaccuracies of that of defendants. *See* R. STERN & E. GRESSMAN, SUPREME COURT PRACTICE, §§ 6-44, 11-9 (3d ed. 1962).

Defendants incorrectly assert that one of plaintiffs' claims of a misleading statement stems from an "omission to advise the plaintiffs that Rule 144 would not be 'available as an exemption from the registration requirements of the Securities Act of 1933' if JBI did not make available certain information required under

2. Contrary to Supreme Court Rule 23(c), defendants have not stated the question presented for review, but rather rephrased the considerations which they contend support the issuance of a writ of certiorari. *See* R. STERN & E. GRESSMAN, SUPREME COURT PRACTICE, § 6-42, at pp. 248-249 (3d ed. 1962). Plaintiffs have accordingly set forth the actual issue which the Court is requested to review if it issues the writ.

3. The tenor of defendants' approach is illustrated by their gratuitous and irrelevant reference to other litigation between members of defendants' and plaintiffs' families.

Rule 15c2-11 of the Securities Exchange Act." (Petition, p. 5.) In fact, as the Complaint clearly demonstrates, and as the court of appeals recognized,[4] plaintiffs' claim is that the Information Statement was misleading because of the ambiguous statements concerning the potential availability of Rule 144 when Rule 144 was not in fact available to JBI stockholders. (Complaint, ¶ 10 (b), 21a-22a.)

With respect to the second claim of misleading statements, defendants again inaccurately describe the plaintiffs' position. Plaintiffs do not contend, as defendants assert, that the Information Statement is misleading for failing to disclose that rights appurtenant to the stock of the operating companies under Illinois law would materially differ in four particular respects from rights appurtenant to the stock of JBI under Delaware law. (Petition, p. 7.) Rather, the plaintiffs' Complaint alleges that the Information Statement was misleading as a result of its purported description of the newly-issued capital stock of JBI. (Complaint, ¶ 10c, 22a.) The Information Statement affirmatively revealed certain shareholders' rights that would be affected, but no disclosure was made of other material differences in rights appurtenant to the stock of the operating companies and rights appurtenant to JBI stock which could have adverse consequence for plaintiffs.

Defendants' Statement of the Case also discusses matters that the Complaint does not allege, stating as follows:

> The complaint is devoid of any allegation which indicates how the alleged hypothetical difference between Illinois and Delaware Corporation Law are related to the facts of this case in any way, nor does the complaint allege or suggest that any action was planned or subsequently occurred which would be affected by such alleged difference.

(Petition, p. 8.) This statement is not only argumentative, but it is totally specious. Hindsight may, of course, be illuminating, but it is absolutely irrelevant to this action in which plaintiffs

4. *See* 571 F. 2d at 705, 707 (6a, 8a).

seek relief pursuant to Section 10(b) of the Securities Exchange Act of 1934, 15 U. S. C. § 78j(b) (1970). Plaintiffs need not establish what occurred subsequent to the illegal securities transaction since the crux of a Section 10(b) action is the use of any manipulative or deceptive device in connection with the purchase or sale of security.[5] If defendants' position had any merit it would mean that a valid Section 10(b) claim could never arise until it is possible to determine whether the undisclosed event actually occurs. Such a result is totally at odds with the purpose of the securities laws.[6]

Perhaps the most crucial omission in the defendants' Statement is the failure to recite the procedural posture of this case and to note the Second Circuit's limited holding in light of that posture. The case is not at issue. Rather the defendants filed a Motion to Dismiss pursuant to Rules 12(b)(6) and 9(b) of the Federal Rules of Civil Procedure for failure to state a claim upon which relief can be granted and for failure to plead with particularity the circumstances constituting fraud. District Court Judge Milton Pollack granted that motion under both Rules.[7] On appeal the Second Circuit held that plaintiffs' Complaint complies with the requirements of Rule 9(b) and that plaintiffs' second and third allegations of misleading statements constitute valid claims which, if proven, warrant relief being granted to plaintiffs. The Second Circuit expressed no view on the merits of this case, properly noting it would be premature to do so, and that the question of "materiality should not ordinarily be disposed of on a Rule 12(b)(6) motion". 571 F. 2d at 707.

5. *See Rochelle* v. *Marine Midland Grace Trust Co.*, 535 F. 2d 523, 532 (9th Cir. 1976); *Tomera* v. *Galt*, 511 F. 2d 504, 510 (7th Cir. 1975); *Shapiro* v. *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 495 F. 2d 228, 235 (2d Cir. 1974).

6. *See, e.g., Affiliated Ute Citizens* v. *United States*, 406 U. S. 128 (1972); *Glen-Arden Commodities, Inc.* v. *Costantino*, 493 F. 2d 1027 (2d Cir. 1974). Similarly, defendants' reference to an absence of an attack by the plaintiffs on the fairness of the stock exchange (Petition, p. 5) is not a relevant consideration to plaintiffs' Section 10(b) action.

7. The district court's opinion, however, is devoid of any discussion as to how or why the Complaint failed to comply with Rule 9(b).

REASONS WHY THE WRIT SHOULD BE DENIED.

A. The Decision Below Was Correct and Does Not Contravene This Court's Decision in TSC Industries, Inc. v. Northway, Inc.

Contrary to defendants' contention the decision below is fully in accord with this Court's decision in *TSC Industries, Inc.* v. *Northway, Inc.*, 426 U. S. 438 (1976). In fact, in defining the issue presented by this case, the Second Circuit explicitly employed the standard of materiality as set forth in *TSC*:

> The issue on this Rule 12(b)(6) motion is whether the plaintiffs can prove any set of facts that, had they been disclosed, would have been considered by the reasonable shareholder to have "significantly altered the 'total mix' of information made available." *Id.* [*TSC*] at 449, 96 S. Ct. at 2133.

571 F. 2d at 707 (8a). Applying that standard to the plaintiffs' Complaint, the Second Circuit correctly held:

> The statements about the availability of Rule 144 and the omissions regarding Delaware law raise substantial issues. The statement about the potential availability of Rule 144 could have misled the reasonable shareholder into thinking that it was, in fact, available to him. Similarly, the discussion of the loss of preemptive rights and the discontinuance of cumulative voting as a result of the changeover to Delaware law, could have misled him into thinking that the changeover did not otherwise affect his rights.

Id. (8a-9a.)

Defendants, however, suggest that the Second Circuit's use of the word "could" instead of "would" is an affront to this Court's *TSC* materiality standard and will engender a magnitude of meritless litigation and transform proxy statements into avalanches of trivial information. (Petition, pp. 9-14.) This parade of imaginary horribles understandably ignores the procedural

posture of this case on a motion to dismiss. This Court has held that a complaint will not be dismissed unless it appears to a certainty that the plaintiff is not entitled to relief under any state of facts which could be proven in support of the claim. *See, e.g., Conley* v. *Gibson*, 355 U. S. 41 (1957). Recognizing this long standing rule, the Second Circuit applied the materiality standard in a manner consistent with federal procedure as well as federal securities law,[8] stating:

> On this motion to dismiss for failure to state a claim, plaintiffs' allegations must be accepted as true and must be read in the manner most favorable to them. This is especially true when dealing with questions of materiality which, since they are "mixed questions of law and fact," require delicate assessments of the inferences a "reasonable shareholder" would draw from a given set of facts and the significance of those inferences to him, and these assessments are peculiarly ones for the trier of fact. *TSC Industries, Inc.* v. *Northway, Inc.*, 426 U. S. 438, 450, 96 S. Ct. 2126, 2133, 48 L. Ed. 2d 757 (1976).

571 F. 2d at 706-707 (8a) (footnote omitted).

The Second Circuit's use of the word "could" rather than "would" only demonstrates the court's cognizance of the procedural posture of the case—defendants sought a determination of the materiality of misstatements and omissions based upon

8. Unlike this case, *TSC* involved a summary judgment motion and very different principles than a motion under Rule 12(b)(6) of the Federal Rules of Civil Procedure. In fact, defendants err in their Petition when they characterize the *TSC* holding as follows:

> [A]n omitted fact is material only if there is a "substantial likelihood that under all circumstances the omitted fact would have assumed actual significance in the deliberations of a reasonable shareholder".

Petition at 9-10. An accurate characterization of this Court's holding is:

> An omitted fact is material *as a matter of law* only if there is a substantial likelihood that under all circumstances the omitted fact would have assumed actual significance in the deliberations of a reasonable shareholder.

See 426 U. S. at 450, 453 (emphasis added).

the Complaint only. Other courts applying the *TSC* standard have also recognized that the materiality test must not usurp the role of the trier of fact.[9] *See Billet* v. *Storage Technology Corp.*, 72 F. R. D. 583, 586 (S. D. N. Y. 1976); *Imperial Supply Co.* v. *Northern Ohio Bank*, 430 F. Supp. 339, 357 (N. D. Ohio 1976). *See also Alton Box Board Co.* v. *Goldman, Sachs & Co.*, 560 F. 2d 916, 922 (8th Cir. 1977); *May Department Stores Co.* v. *First Hartford Corp.*, 435 F. Supp. 849 (D. Conn. 1977).

Moreover, to suggest, as the defendants do (Petition, p. 13), that the Second Circuit's use of "would" is tantamount to an adoption of the prior "might" standard rejected by this Court in *TSC*, ignores the very historical underpinnings of the *TSC* decision. The Second Circuit opted for the "would" standard more than three years prior to this Court's resolution of the conflict among the courts of appeals over the "would" versus "might" standard as this Court observed in *TSC*. *See TSC Industries, Inc.* v. *Northway, Inc.*, 426 U. S. 438, 445, 449 (1976), *citing with approval, Gerstle* v. *Gamble-Skogmo, Inc.*, 478 F. 2d 1281 (2d Cir. 1973). *See also Gould* v. *American-Hawaiian S. S. Co.*, 535 F. 2d 761, 770 (3d Cir. 1976). The Second Circuit merely applied its own standard, as ratified by this Court, in disposing of the appeal in this case.

Finally, defendants' contention that the decision below will open the floodgates to meritless securities litigation cannot withstand analysis. As indicated, the Second Circuit's opinion is a well-reasoned decision based upon long-standing legal principles in the securities field and that of federal procedure. Moreover, the decision involves two well-defined factual areas in which the Second Circuit held that a cause of action had been stated: (1) the suggestion of an exemption from registration under the federal securities laws pursuant to Rule 144; and (2) the failure of having disclosed some significant differences on shareholders' rights resulting from the reorganization, to disclose other significant differences or to avoid all reference to any differences.

9. Plaintiffs have demanded a trial by jury. *See* Complaint (25a).

To the extent that analogous situations arise, it is specious to suggest that they will constitute an avalanche. Moreover, contrary to defendants' assertion, the Second Circuit's decision will tend to diminish rather than expand information since the vice in defendants' disclosure was that they said more than what was required out of a desire to further their proposed reorganization. Having done so, it was incumbent upon them to close the disclosure circle. The prudent person who reads the Second Circuit's decision will be less inclined, not more inclined, to include information, trivial or otherwise, that is not material out of a desire to mislead investors.

B. The Second Circuit's Opinion Does Not Conflict with Decisions in Other Circuits.

Defendants assert that the Second Circuit's opinion conflicts with decisions of the Third and Fifth Circuit because of its failure to note two cases cited by the district court, *Ash* v. *LFE Corp.*, 525 F. 2d 215 (3d Cir. 1975); *Vohs* v. *Dickson*, 495 F. 2d 607 (5th Cir. 1974). Those cases, however, are inapposite to this case and the Second Circuit had no reason to discuss them.

Ash and *Vohs* presented a very different legal issue than the one raised by this case. In both cases the courts of appeal were asked to decide whether a material omission resulted from the complete failure of the seller of the securities in question to disclose a "legal theory" or to render "legal advice" to the buyer. In contrast, the issue in this case is whether the Information Statement was misleading in disclosing some of the changes in the stockholders' rights that would occur if the Plan was adopted, but not other changes that might have an adverse effect on the shareholders' control of future important corporate decisions.

Plaintiffs do not contend that defendants had a duty to disclose the differences in the two states' corporation laws. Had the

Information Statement done nothing more than inform the shareholders that the new holding company, JBI, was to be incorporated under the laws of Delaware rather than Illinois where all of the operating companies were incorporated, there would be no claim. Rather, the Complaint alleges that the Information Statement purported to describe the newly-issued stock by disclosing in detail the following differences:

Illinois Law	*Delaware Law*
(a) cumulative voting required	(a) no cumulative voting
(b) preemptive rights	(b) no preemptive rights
(c) dividends paid annually	(c) dividends to be declared and paid at the discretion of the Board

However, the Information Statement failed to disclose the following differences at all:

Illinois Law	*Delaware Law*
(a) two-third voting requirement for mergers, amendments to Articles of Incorporation, dissolution, etc.	(a) simple majority voting requirement for mergers, amendments to Articles of Incorporation, dissolution, etc.
(b) Board vacancies required a vote of shareholders in order to be filled	(b) Board vacancies can be filled by JBI directors without shareholders' approval
(c) appraisal rights for dissenting shareholders	(c) no appraisal rights for dissenting shareholders
(d) limited rights of indemnification for corporate officers and directors	(d) broad rights of indemnification for corporate officers and directors

Such a limited description of the differences in shareholders' rights, in light of the omission of others, was certainly misleading by lulling the investors into believing that all of the pertinent differences had been disclosed. Thus, a partial disclosure of the legal rights of the stockholders, as occurred in this case, presents a very different issue than confronted the *Ash* and *Vohs* courts

where no disclosure whatsoever was made with respect to legal matters.

Not only does this case present a very different legal issue than was raised in *Ash* and *Vohs*, but neither of those cases was decided on a motion to dismiss. Moreover, those cases are factually distinguishable. In *Ash*, the plaintiff alleged that a management proxy solicitation was misleading with respect to a proposed employee pension plan. The claim was premised upon plaintiff's belief that certain of the pension plan's benefits constituted a "gift" under Delaware law and that the proxy failed to clearly disclose the proposed plan's increased benefits for management. Unlike the partial disclosure by the Information Statement in this case, the proxy in *Ash* did state the rate of compensation under both the prior pension plan and the proposed plan. All it failed to do was to make the simple arithmetical computation to show the amount of increase that management would receive if the proposed plan were adopted.

The *Vohs* case was an action by buyers of unregistered stock of their corporate employer against the seller, a co-employee. The seller had no more knowledge of securities law than the buyers and the sale was thus an isolated transaction exempt from Georgia registration requirements. The *Vohs* court specifically held that an "ordinary employee-stockholder is not chargeable with constructive knowledge of financial matters he might have discovered by an expert review of company books." 495 F. 2d at 624. In contrast to the *Vohs* situation, the individual defendants in this case were not ordinary stockholders unknowledgeable of securities law. Rather, they were officers of and legal counsel for JBI who actually prepared the Information Statement. Moreover, William Collier occupied the dual role as counsel for JBI and the personal attorney of plaintiff William Joyce. Clearly, neither the *Ash* nor the *Vohs* decision is in conflict with that of the Second Circuit.

CONCLUSION.

Notwithstanding defendants' rhetoric, this is not a case which warrants the exercise of this Court's discretion in issuing a writ of certiorari. Defendants' quarrel is with the correctness of the decision, but that issue does not warrant review by this Court. In advancing that quarrel they have sought to turn the small rock of this decision below into an avalanche of litigation, and cases involving different legal issues, procedural postures and facts into a conflict in circuits. Their alchemy falls far short of the mark.

It is respectfully submitted that the decision of the Second Circuit holding that plaintiffs have stated a cause of action against defendants under Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 faithfully and accurately applied this Court's *TSC* decision. Nothing in the decision below is in conflict with either the *Ash* or *Vohs* decision. The Petition should accordingly be denied.

Respectfully submitted,

DONALD E. EGAN,
LEE ANN WATSON,
KATTEN, MUCHIN, GITLES,
ZAVIS, PEARL & GALLER,
55 East Monroe Street,
Suite 4100,
Chicago, Illinois 60603,
Attorneys for Respondents.